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NO. 85-1395

IN THE

Supreme Court of the United States

October Term, 1985

NATIONAL STEEL CORPORATION,
Petitioner,
v.
PUBLIC SERVICE COMMISSION OF
WEST VIRGINIA,
Respondent.

On Petition for a Writ of Certiorari
to the Supreme Court of Appeals
of West Virginia

BRIEF OF RESPONDENT PUBLIC SERVICE COMMISSION OF WEST VIRGINIA IN OPPOSITION

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QUESTION PRESENTED FOR REVIEW

Whether the Public Service Commission of West Virginia, in establishing a methodology for cost recovery by a state regulated public utility, failed to provide sufficient notice of such methodology in violation of the Fourteenth Amendment of the United States Constitution.

MISCELLANEOUS

Re: Columbia Gas of West Virginia, Inc., Case Nos. 80-336-G-30C and 81-366-G-30C, 47 PUR 4th 392, (1982), 69 ARPSCWV 633 (1982) 9

Re: Columbia Gas of West Virginia, Inc., Case No. 82-739-G-30, _____ARPSCWV_____, (1983) 9

Rules and Regulations for the Government of the Construction and Filing of Tariffs of Public Utilities and Common Carriers by Motor Vehicle.....3

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The respondent, the Public Service Commission of West Virginia, herewith opposes the petition for a writ of certiorari to the Supreme Court of Appeals of West Virginia filed by the petitioner, National Steel Corporation.[1]

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[1]Pursuant to Rules 22 and 34.2, respondent adopts the portions of the petition filed in response to Rule 21.1(b), (d), (e), and (f).

ADDITIONAL STATUTORY PROVISIONS

West Virginia Code §24-1-1 provides in pertinent part:

> (a) It is the purpose and policy of the legislature in enacting this chapter to confer upon the public service commission of this State the authority and duty to enforce and regulate the practices, services and rates of public utilities in order to:
>
> ***
>
> (4) Ensure that rates and charges for utility services are just, reasonable, applied without unjust discrimination or preference and based primarily on the costs of providing these services; . . .
>
> ***
>
> (b) The legislature creates the public service commission to exercise the legislative powers delegated to it. The public service commission is charged with the responsibility for appraising and balancing the interests of the State's economy and the interests of the utilities subject to its jurisdiction in its deliberations and decisions.
>
> (c) The legislature directs the public service commission to identify, explore and consider the potential benefits or risks associated with emerging and state-of-the-art concepts in utility management, rate design and conservation.

STATEMENT OF THE CASE

The petition filed in this case arises out of a proceeding before the Public Service Commission of West Virginia (Commission), Case No. 83-348-G-30C. This case was

filed by Columbia Gas of West Virginia (Columbia)[2] to pass through to its customers purchased gas costs pursuant to the Commission's purchased gas adjustment (PGA) procedure, commonly known as Rule 30-C.[3] In order to understand the factual situation which gave rise to the subject case, it is helpful to review the history and the purpose of Rule 30-C.

BACKGROUND

Natural gas utilities in West Virginia charge rates for gas service that are composed of two parts. Approximately 20% of the rate relates to costs incidental to the ability to maintain and operate the gas utility. The remaining 80% of the rate is the direct result of costs involved in procuring the gas commodity from a wholesale or other supplier, and may include a combination of demand costs (fixed costs) and commodity costs (variable costs) depending on the size of the natural gas utility.

By General Order No. 183.4, entered on June 26, 1979,

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[2]At the time of the filing, Columbia sold natural gas at retail in the State of West Virginia. Columbia purchased its gas supplies almost exclusively from Columbia Gas Transmission Corporation, an entity whose rates and charges are regulated by the Federal Energy Regulatory Commission.

[3]Rule 30-C of the Commission's *Rules and Regulations for the Government of the Construction and Filing of Tariffs of Public Utilities and Common Carriers by Motor Vehicle* is a voluntary accelerated rate procedure available to natural gas utilities subject to the jurisdiction of the Commission. Rule 30-C provides a mechanism whereby gas utilities may recover increases in the cost of gas purchased from their suppliers in a more timely fashion than would be possible in a general rate proceeding. The complete text of Rule 30-C, as amended in 1979, can be found in Appendix E, page 65a, of the Petition for Writ of Certiorari filed by National.

the Commission adopted several changes in the then existing Rule 30-C mechanism. One of these changes involved the cessation of the use of monthly purchased gas adjustments and the adoption of a levelized annual adjustment. This change was initiated due to concerns over monthly fluctuations in gas rates that proved confusing to customers. The effect of this change was to allow gas utilities to file in August of each year an estimate of purchased gas costs for the annual period beginning November 1. Included with the application is a statement of actual purchased gas costs, including any over or underrecovery, and refund information for the previous twelve months ending June 30. After review of this data and a hearing, if necessary, the Commission issues an order which allows the utility to recover prospectively a purchased gas cost composed of three elements: *estimated* gas costs for the ensuing twelve months; an *actual* cost adjustment (ACA) for over or underrecoveries of purchased gas costs for previous periods; and applicable adjustments for taxes and unaccounted for gas. It is the method of recovering the actual cost adjustment amount that is at issue in this proceeding.

THE CASE BELOW

The instant case arises out of the aforesaid Rule 30-C proceeding before the Public Service Commission. On August 10, 1983, Columbia filed an application with the Commission to change rates for natural gas service in compliance with Rule 30-C. The application was designated as Case No. 83-348-G-30C, and by order entered on September 21, 1983, a prehearing conference was scheduled to establish the identities of the parties, the issues to be addressed, and the procedural schedule to be followed.

As a result of the prehearing conference, an order was

issued on October 13, 1983, setting an interim hearing for October 24, 1983, for the purpose of establishing interim rates, with the final substantive hearings to begin on January 9, 1984.

On October 24 and 25, 1983, the interim hearings were conducted and on November 14, 1983, an interim purchased gas cost was established. After the advance filing of direct and rebuttal testimony by all parties, hearings were held on January 9 and 11, 1984, on the case in chief. At the conclusion of these hearings, parties submitted simultaneous initial and reply briefs on all relevant issues.

On October 31, 1984, the Commission entered an order approving the interim rates and adopting a modified method of recapturing prior period underrecoveries by ordering Columbia to directly bill each customer in the LV-1, LV-2, IUS-1 and IUS-2 rate schedules for any underrecovery balances, or to refund to such customer any overrecovery balance.

After reviewing petitions for reconsideration filed by several parties, the Commission issued its December 28, 1984 Order on Petition for Reconsideration, which modified the October 31, 1984 Order by changing the beginning date for calculating the comprehensive balance to July 1, 1980 and providing for payments or refunds to be made on a prospective basis in twelve equal monthly installments, without interest, after receiving notification of the account balance.

On January 28, 1985, National appealed the Commission decision to the Supreme Court of Appeals of West Virginia. A similar petition was filed by Westvaco Corporation, another party to the proceeding. After briefing and oral argument thereon, the Supreme Court of Appeals of West Virginia, by majority vote, denied the appeals without opinion on April 23, 1985.

While the appeals were pending in the Supreme Court of

Appeals of West Virginia, and subsequent to that Court's refusal to grant an appeal, the Commission issued several further orders in the case which were designed to clarify the effect of the October 31, 1984, and December 28, 1984, Orders. The first such Order, entered on February 28, 1985, rejected the calculations filed by Columbia's successor, Mountaineer Gas Company,[4] and ordered the Commission's Staff to calculate the appropriate balances by March 20, 1985. The Order provided all interested parties an opportunity to file comments by April 4, 1985, which period was subsequently extended to April 12, 1985.

By Order entered April 24, 1985, the Commission approved the Staff calculations and reinstated the payment obligations. On May 3, 1985, Mountaineer Gas Company requested that it be authorized to collect business and occupation taxes on outstanding balances. On May 17, 1985, National filed a motion for a reopening of the comment period on the Staff's calculations of over or underrecovery balances.

On June 13, 1985, the Commission reopened the comment period through June 24, 1985, and authorized the collection of applicable taxes on outstanding account balances. The comment period was subsequently extended through July 1, 1985.

Comments on the matter were submitted by Westvaco Corporation and National on June 24, 1985 and July 1, 1985, respectively. National also filed a petition for reopening and reconsideration.

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[4]On May 25, 1984, the Commission entered an Order approving the acquisition of all the common stock of Columbia Gas of West Virginia by Allegheny and Western Energy Corporation, which resulted in Columbia being renamed Mountaineer Gas Company. It is Mountaineer Gas Company that will be sending the direct bills to the Petitioner.

On July 10, 1985, the Commission issued a Final Order in the proceeding denying National's petition for reopening and reaffirming in all substantive parts the Commission's position as enunciated in the October 31, 1984, and December 28, 1984, Orders.

On August 9, 1985, National again appealed the Commission's Orders to the Supreme Court of Appeals of West Virginia. A similar petition was filed by Westvaco Corporation and by a group of industrial customers of Columbia. After briefing and oral argument, the Supreme Court of Appeals of West Virginia unanimously rejected the appeals without opinion on November 6, 1985.

REASONS FOR DENYING THE WRIT

The Petitioner in this case contends that the Commission has committed two acts repugnant to the due process requirement of the Fourteenth Amendment to the United States Constitution. First, it is contended that the Commission failed to follow its administrative rules; second, the Petitioner asserts that the Commission's decision results in retroactive ratemaking. Each contention is without merit.

The Petitioner has failed to demonstrate a justification for further review of the Commission's decision by this Court. As will be demonstrated below, the actions of the Commission are consistent with its statutory responsibilities and do not conflict with relevant decisions of this Court or other courts and administrative agencies.

I. The Commission's Actions Were Consistent With The Intent And Prior Application Of Rule 30-C

The Petitioner has alleged that this proceeding was tainted by the failure of the Commission to follow its ad-

ministrative rules. The Commission believes that its decision in this proceeding conforms to both the intent and prior application of Rule 30-C.

As has been previously mentioned, Rule 30-C is an optional, expedited method of rate recovery that is limited in its application to the recovery of purchased gas costs. By its very nature, and the fact that it contains no provision allowing for the recovery of any revenues associated with base rates,[5] Rule 30-C merely serves the purpose of truing up gas costs with revenues received. Under Rule 30-C a gas utility is allowed to recover its actual, prudently incurred purchased gas costs through a purchased gas adjustment rate. That rate contains an estimate of future purchased gas costs plus an actual cost adjustment for purchases made in previous periods. In some cases the ACA amount may be an overrecovery, which results in a reduction in the purchased gas adjustment. During periods in which the utility does not collect its actual purchased gas costs, an underrecovery results, and that amount is added to the purchased gas adjustment calculation. Despite what the Petitioner's have alleged, Rule 30-C has worked in that fashion since its amendment in 1979. At the end of every period there is invariably a net overrecovery or underrecovery that is carried forward to the next period.

Therefore, Rule 30-C serves both as a guide to predicting the future cost of gas purchased by a public utility from its suppliers and as a mechanism for truing up revenues with actual gas costs. One of the underlying premises is that the estimated rates approved in November of each year may be more or less than the actual future cost of gas; consequently, the rate is later adjusted

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[5]The Commission uses the terminology "base rate" to describe the approximately 20% of the total gas rate that is related to the non-commodity costs.

through the use of the ACA mechanism to ensure that the utility is receiving its actual, prudently incurred gas costs. This adjustment is necessary because Columbia's principal wholesale gas supplier routinely changes its purchased gas cost rate every six months, while Columbia is allowed under Rule 30-C to make only one such change per year. During periods of rapidly escalating gas prices and diminishing retail customer usage, as was experienced during the period covered by the instant proceeding, under-recovery of gas costs is almost a certainty. For that reason, the ACA plays an important role by ensuring that the utility is made whole for costs it has incurred by truing up the balances between costs and revenue recovery.

In promulgating Rule 30-C, the Commission realized that it could not be routinely applied to every gas utility in West Virginia, due to the varying sizes and purchasing practices of the more than forty-one gas utility companies operating in the State. Therefore, the Commission has treated Rule 30-C as a vehicle for establishing the minimum filing requirements necessary for the accelerated recovery of purchased gas costs, while reserving for itself, in the preamble of the Rule, sufficient discretionary powers to allow the Commission to tailor the application of the Rule to the exigencies of the particular utility under review:

> The Public Service Commission of West Virginia may interpret this rule if necessary and may require appropriate action based upon any such interpretation. The Commission reserves the authority under its general power to review any information filed under this rule and to order appropriate changes based on applications before the Commission. If any provision of this rule would result in undue hardship for a utility or its customers, the Commission may modify the ap-

plication of this rule appropriately. (Rule 30-C, Petitioner's appendix, page 71a)

The Petitioner claims that the instant Rule 30-C proceeding was not "normal" in that the Commission did not strictly adhere to the literal language of Rule 30-C. The Petitioner is aware, however, that no Columbia Rule 30-C case since the amendment of the Rule in 1979 has strictly followed the literal language of the Rule. Instead, the Commission has exercised the power it reserved to modify the application of the Rule on a case-specific method to prevent undue hardship. For example, in Columbia Case Nos. 80-336-G-30C and 81-366-G-30C, 47 PUR 4th 392, (1982), the Commission modifed the application of the Rule to allow a calculation of over or underrecoveries by customer class based on monthly sales. In Columbia's next filing, Case No. 82-378-G-30C, _____ ARPSCWV _____, (1983), the Commission adopted a further modification of the application of the Rule to allow demand costs to be tracked according to customer classes. The instant filing simply went the next logical step in cost recovery by requiring that gas costs be directly recovered from the customer causing the utility to incur the cost. In each of the cases in which the application of the Rule was modified the Petitioner was granted intervenor status and actively participated in the proceeding. Therefore, the Petitioner knew that it was common practice for the Commission to modify its Rule from case to case.

In all other respects the instant proceedings was unexceptionable. Pursuant to Commission Order and *West Virginia Code* §24-2-4a, notice of the proposed purchased gas increase was published as a Class II legal advertisement in every county in which Columbia did business. This notice afforded customers an opportunity to file their protests with the Commission or to seek status as in-

tervenors in the proceeding. The Petitioner in this case belonged to the clearly identifiable large volume industrial usage class. Although Petitioner's individual gas purchases from Columbia were purportionately higher than those for other customers, there is no statutory requirement that individual or actual notice be given to each customer of a proposed rate increase. Indeed, it is because of the Petitioner's large usage of gas that such notice is unnecessary. This Court should recognize that the Petitioner is not an unsophisticated customer victimized by inadequate notice, but a customer that knows not only what a Rule 30-C proceeding entails, but also that every gas utility company in West Virginia makes such a filing annually. Many large volume customers have entire departments that do nothing more than track the usage and cost of energy, and are exceedingly knowledgeable in the way the Commission handles gas cost proceedings.

Due process imposes constraints on governmental decisions which deprive individuals of certain "liberty" or "property" rights by requiring that some form of hearing be held before an individual is finally deprived of a property interest. *Wolfe v. McDonnell,* 418 U.S. 539, (1974). In *Memphis Light, Gas and Water Division v. Willie S. Craft,* 436 U.S. 1, (1978), this Court did not require a full evidentiary proceeding to satisfy due process standards as long as some informal administrative proceeding was available. Certainly, in this proceeding the opportunity afforded the Petitioner to present its arguments far exceeded the requirements of *Craft, supra.* For example, on October 5, 1983, the Commission held a prehearing conference to identify the parties and the issues to be addressed, at which time the Petitioner appeared by counsel. The Petitioner also participated in the interim hearings on October 24 and 25, 1983, and the final, substantive hearing on January 9 and 11, 1984, by presenting testimony,

cross-examining witnesses and filing a brief in opposition to the direct billing mechanism.

The Petitioner in this proceeding may not have liked the direct billing concept, but it can not truthfully claim that it was "surprised" by it or afforded an inadequate opportunity to challenge the decision. (Petition, p. 18) First, the issue of the substantial underrecovery in the large volume customer classes was a recurring area of concern. The amount of the underrecovery was clearly discernible by a review of Columbia's Rule 30-C application.[6] Similar information had been available to the Petitioner in each of Columbia's prior Rule 30-C filings. The Staff's direct testimony, filed on October 14, 1983 in the interim phase of the proceeding, specifically noted that the Commission might want to modify the application of the actual cost adjustment, but should defer that decision to the January case in chief proceedings. At that time, more than a year before the Commission's October 31, 1984 Final Order, the Petitioner should have been on notice of the possibility of modified application of the Rule. Indeed, on December 29, 1983, the staff filed its direct testimony in which the concept of direct billing of prior period underrecoveries was clearly presented. The Petitioner's claim that direct billing ". . . was not mentioned until near the end of the proceedings when it was injected into the case in the rebuttal testimony of a member of Resondent's Staff . . ." is simply untrue. (Petition, pp. 17, 18) The Petitioner was aware of the Staff's testimony two weeks prior to the final hearings and had ample opportunity to file testimony in

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[6]Columbia's Rule 30-C filing on Schedule No. 3, Sheet 2 of 7 showed a cumulative underrecovery balance for the twenty-four month period ended June 30, 1982 of over $5,000,000, which was directly attributable to underrecoveries in the large volume industrial customer classes.

opposition, cross-examine the Staff's witness or request futher hearings on the issue.

This "surprise" testimony did not create a "sudden" conflict for Petitioner's legal counsel, as has been claimed. (Petition, p. 18) The record will reflect that counsel for Petitioner vehemently opposed the direct billing concept, believing that it would be detrimental to his client's interests. In any event, although the closing date of the sale of the Weirton Steel Division of National Steel Corporation was officially on January 11, 1984, Weirton had been operated for the account of the prospective purchaser, Weirton Steel Corporation, as of May 1, 1983. Obviously, the Petitioner had adequate time to have obtained necessary counsel had it so desired.

II. The Commission's Decision Requiring The Petitioner To Pay Nothing More Than The Actual Cost For Services Rendered Does Not Constitute Retroactive Ratemaking.

It should be noted at the outset that although the petition for a writ of certiorari is based on an alleged denial of due process, the Petitioner did not strongly assert that issue before the Supreme Court of Appeals of West Virginia. Indeed, the petition for appeal filed by the Petitioner in that Court contained only slightly more than one full page of argument on that issue. Instead, the Petitioner focused on a claim under West Virginia law that the Commission's action in authorizing direct billing of prior period underrecoveries constitutes an impermissible attempt to recover "past losses" retroactively.[7] The West

[7]The Commission believes that the issue of retroactivity is a state issue involving the application of state statutory law and the regulations of a state agency which were reviewed by the state supreme court, and, therefore, does not present a federal question. In any event, the Commission did not engage in retroactive ratemaking.

Virginia Supreme Court of Appeals has addressed the area of retroactive ratemaking on several occasions. In *Chesapeake & Potomac Telephone Company of West Virginia v. Public Service Commission,* _____ W.Va. _____, 300 S.E.2d 607, 619, (1982) (rehearing denied, 1982), the Court expounded upon the Commission's statutory ratemaking authority:

> This concept (of acting prospectively) is inherent in the statute establishing the general power of the Commission to ". . . affix reasonable rates . . . to be followed in the future." *West Virginia Code* §24-2-3 (1980 replacement volume). Generally, retroactive ratemaking occurs when a utility is permitted to recover an additional charge for past losses, or when a utility is required to refund revenues collected, pursuant to then lawful rates.

The Commission in its Statement of Reasons for the Entry of Order, filed in accordance with Section 24-5-1 of the Public Service Commission Law, *West Virginia Code* §24-5-1, stated to the Supreme Court of Appeals of West Virginia that direct billing of underrecoveries did not result in the recovery of any "past losses." Indeed, allowing direct billing would have no effect on the utility's net revenues, nor would it allow the utility to increase its rate of return or profit levels. The Commission explained to the Court the source of the underrecoveries, and showed the Court that the underrecoveries were nothing more than costs Columbia had incurred directly for the benefit of the Petitioner and other large volume users. These costs related to actual gas consumption and represented nothing more than a truing up of actual purchased gas costs with the amount recovered through the PGA rate. As such, it is not covered by the prohibition on retroactive ratemaking,

recover traceable prior period costs has also been adopted by the Federal Energy Regulatory Commission in *Transcontinental Gas Pipe Line Corporation,* 32 FERC §61,230 (1985). In that case, nearly $127,000,000 in prior period production related costs, dating back to 1980, were directly billed to customers under a method similar to that employed by the Commission.

The Petitioner has not been deprived of its property without due process of law. The Petitioner knew that it was paying estimated rates subject to an annual matching of costs and revenues, and should be required to pay the actual cost for gas services rendered.

CONCLUSION

The petition raises no question warranting plenary review by this Court of the Supreme Court of Appeals' orders denying review of the Commission's action requiring direct billing of underrecoveries based on actual costs for purchased gas. The petition should be denied.

Respectfully submitted,

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